

Message Text

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PAGE 01 STATE 257915

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FM SECSTATE WASHDC

TO AMEMBASSY ABU DHABI

C O N F I D E N T I A L STATE 157915

E.O. 11652:

TAGS:

SUBJECT:

FOLLOWING IS A REPEAT

QUOTE

O 200221Z JUL 74

FM SECSTATE WASHDC

TO AMEMBASSY KUWAIT IMMEDIATE

AMEMBASSY JIDDA IMMEDIATE

C O N F I D E N T I A L STATE 157915

E.O. 11652: GDS

TAGS: ENRG, KU

SUBJECT: HIGH OIL PRICES

REF: KUWAIT 3018

FOLLOWING IS PRIMARILY FOR EMBASSY'S USE. HOWEVER, SECY
SIMON MAY WISH TO DRAW UPON IT IN HIS DISCUSSION OF THE
SUBJECT WITH KUWAITIS.

1; THE DECISION BY GULF AND BP TO ACCEPT KUWAITI DEMANDS
ON BUYBACK PRICES WILL CLEARLY BE A FOCAL POINT OF YOUR
VISIT. WE UNDERSTAND THAT THE COMPANIES HAVE AGREED TO PAY
94 PERCENT OF POSTED PRICE (DOLS 10.85) FOR BUYBACK OIL FOR
THE FIRST FIVE MONTHS OF 1974 AND 94.8 PERCENT (DOLS 10.95)
FOR THE NEXT FOUR MONTHS. OUR PRELIMINARY CALCULATIONS
SUGGEST THAT THIS AGREEMENT WILL INCREASE AVERAGE KUWAIT

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PAGE 02 STATE 257915

CRUDE BY 10-15 CENTS A BARREL. THIS FIGURE WILL RISE IF THE COMPANIES TRY TO RECOVER IN FUTURE SALES THE QTE LOSSES UNQTE MADE ON PAST TRANSACTIONS WHEN THEY WERE COMPUTING BUYBACK PRICES AT 93 PERCENT OF POSTING.

2. WE ARE CONCERNED THAT THIS BUYBACK AGREEMENT WILL STIMULATE A NEW WAVE OF EFFECTIVE PRICE INCREASES IN THE MIDDLE EAST. OTHER PRODUCERS WILL INSIST ON TERMS THAT WILL PROVIDE AN EQUIVALENT PER BARREL GOVERNMENT TAKE. THESE PRICE HIKES, COMING ON THE HEELS OF THE RECENT OPEC DECISION TO RAISE ROYALTY TAXES, WILL FURTHER STRAIN THE WORLD ECONOMY. AS YOU KNOW, THE INCREASES RUN CONTRARY TO CURRENT MARKET CONDITIONS WHICH INDICATE THAT OIL PRICES SHOULD BE FALLING.

3. WHILE WE AGREE WITH REFTEL THAT YOUR VISIT TO KUWAIT SHOULD ACCENTUATE OUR COMPLEMENTARY INTERESTS AND OUR DESIRE FOR A NEW COOPERATIVE RELATIONSHIP, WE SUGGEST THAT YOU ALSO USE THIS OCCASION TO UNDERLINE OUR STRONG CONVICTIONS THAT WORLD OIL PRICES ARE TOO HIGH AND THAT NEW INCREASES -- SUCH AS THOSE THAT WILL RESULT FROM THE RECENTLY CONCLUDED BUY-BACK AGREEMENTS -- ARE UNWARRANTED. HAVING DONE SO, YOU SHOULD MOVE TO THOSE OTHER AREAS WHERE A COMMON VIEW IS MORE PROBABLE.

4. YOU MAY WISH TO DRAW ON THE FOLLOWING TALKING POINTS IN YOUR DISCUSSIONS WITH KUWAITI OFFICIALS:

--I WISH TO BRING TO THE ATTENTION OF THE KUWAITI GOVERNMENT MY GOVERNMENT'S DEEP CONCERN OVER OIL PRICE DEVELOPMENTS. THIS CONCERN IS BEING EXPRESSED TO OTHER OPEC GOVERNMENTS AS WELL AS YOURS.

--THE UNITED STATES BELIEVES THAT WORLD OIL PRICES ARE ALREADY CRITICALLY HIGH. AS A RESULT, THE WORLD ECONOMY IS STRAINED AND WORLD DEVELOPMENT IS BEING RETARDED. THE DIRECT AND INDIRECT BURDEN OF HIGH OIL PRICES ON THE WORLD'S CONSUMERS IS A HEAVY ONE. THE PLIGHT OF THE DEVELOPING CONSUMER COUNTRIES IS EVEN MORE PRESSING.

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PAGE 03 STATE 257915

-- IN THIS REGARD, WE ARE DEEPLY CONCERNED ABOUT THE NEW BUY-BACK AGREEMENT BETWEEN YOUR GOVERNMENT AND THE COMPANIES OF GULF AND BP. SINCE THE COMPANIES AVERAGE THEIR EQUITY AND PARTICIPATION CRUDE IN DETERMINING THEIR TRANSFER PRICES, THIS INCREASE IN BUY-BACK PRICES WILL BE REFLECTED IN A HIGHER AVERAGE PER BARREL COST.

-- THIS NEW BUY-BACK AGREEMENT CANNOT BE CONSIDERED IN A VACUUM. IT WILL STIMULATE OTHER PRODUCERS TO DEMAND SIMILAR BUY-BACK ARRANGEMENTS OR EQUIVALENT GOVERNMENT TAKE AND THEREBY RAISE THE F.O.B. PRICE ON ALL MIDDLE EAST AND PROBABLY ALL OPEC OIL. THESE NEW INCREASES WILL BE PASSED ON AND COMPOUND THE DIFFICULTIES CONSUMING COUNTRIES FACE IN TRYING TO ADJUST TO THE ENORMOUS AND ABRUPT INCREASES IN OIL PRICES OVER THE PAST EIGHTEEN MONTHS.

--THE RECENT TWO PERCENT OPEC INCREASE -- THOUGH SMALL IN COMPARISON TO PRIOR INCREASES -- WILL ALSO INCREASE WORLD OIL PRICES AND FURTHER STRAIN THE WORLD ECONOMY.

-- ANY PRICE INCREASE AT THIS TIME IS CONTRARY TO CURRENT MARKET DEVELOPMENTS. IN THE LIGHT OF LOWER SPOT AND AUCTION BIDS, STOCK BUILDUPS, AND TANKER SLOW-DOWNS, OIL PRICES SHOULD BE FALLING RATHER THAN RISING.

-- WE BELIEVE CURRENT HIGH PRICE LEVELS ARE IN THE INTEREST OF NEITHER CONSUMERS NOR PRODUCERS. IN THE SHORT RUN, THEY HURT CONSUMERS. BUT IN THE LONG RUN, PRODUCERS WILL ALSO LOSE BECAUSE MAINTENANCE OF HIGH PRICES WILL STIMULATE EVER GREATER RESEARCH AND INVESTMENT INTO ALTERNATIVE SOURCES OF ENERGY AND ALTERNATIVES TO ENERGY USE. THE EFFECT WILL BE TO REDUCE THE TOTAL VALUE THE OIL EXPORTERS RECEIVE OVER THE LIFE OF THEIR PRODUCING FIELDS. THE NEW RESULT WILL BE DISADVANTAGEOUS TO ALL.

-- THE QUESTION OF PRODUCTION IS, OF COURSE, CLOSELY RELATED TO THAT OF PRICING. WHILE WE ARE AWARE OF

CONFIDENTIAL

PAGE 04 STATE 257915

SENTIMENTS AND PRESSURES IN SOME PRODUCER STATES TO

REDUCE PRODUCTION FURTHER, WE BELIEVE THESE PRESSURES SHOULD BE RESISTED IN THE INTEREST OF WORLD ECONOMIC WELL-BEING.

-- IN OUR INTERDEPENDENT WORLD, THE ECONOMIES OF ALL COUNTRIES ARE CLOSELY RELATED. ALL NATIONS, PRODUCERS

AND CONSUMERS, WILL SUFFER IN A WORLD THAT IS CHARACTERIZED BY FALTERING AND FAILING ECONOMIES.

-- WE RECOGNIZE THAT PRODUCING COUNTRIES ARE ANXIOUS TO PROTECT THEIR REAL EARNINGS IN THE CURRENT WORLD-WIDE INFLATION. HOWEVER, THESE COUNTRIES SHOULD ALSO

RECOGNIZE THAT THE TREMENDOUS INCREASES IN OIL PRICES OF THE PAST SEVERAL MONTHS ARE IN THEMSELVES A MAJOR CAUSE OF WORLD INFLATION. THUS, EFFORTS TO OFFSET INFLATION BY RAISING PRICES ARE NOT ONLY SHORTSIGHTED BUT ALSO COUNTERPRODUCTIVE.

-- A RESOLUTION OF DIFFERING VIEWS ON PRICING AND PRODUCTION QUESTIONS IS URGENT AND ESSENTIAL. HOWEVER, AS BOTH SIDES NOW BEGIN TO WORK OUT THESE DIFFICULT BUT NOT INSOLUBLE PROBLEMS, WE BELIEVE IT IS IN THE INTEREST OF PRODUCERS AND CONSUMERS NOT TO LOSE THEMSELVES IN POLEMICS. THIS COULD INHIBIT GROWING AND BENEFICIAL TRENDS TOWARD COMPLEMENTARY FINANCIAL, COMMERCIAL, AND INDUSTRIAL PROGRAMS WHICH HOLD SO MUCH PROMISE FOR ALL CONCERNED, BUT WHICH MUST BE BASED UPON A STABLE SUPPLY OF ENERGY TO THE GLOBAL ECONOMY.

-- TO THIS END, AND IN REALIZATION THAT STABLE SUPPLY AT REASONABLE PRICES IS CRUCIAL TO ANY CONSIDERATION OF ENERGY PROBLEMS, WE HOPE TO ENCOURAGE A DIALOGUE WITH PRODUCER STATES WHICH DOES NOT FOCUS ON OIL PRICES AND PRODUCTION TO THE EXCLUSION OF THE MANY OTHER VERY IMPORTANT ASPECTS OF PRODUCER/CONSUMER RELATIONS.
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